CAPITAL PROJECTS AND BOND OVERSIGHT COMMITTEE

Minutes

December 16, 2003

The Capital Projects and Bond Oversight Committee met on Tuesday, December 16, 2003, at 1:00 PM, in Room 129 of the Capitol Annex. Representative Jodie Haydon, Chair, called the meeting to order, and the secretary called the roll.

Present were:

Members: Senator Robert Leeper, Co-Chair; Representative Jodie Haydon, Co-Chair; Senators Tom Buford, Virgil Moore, and Jerry Rhoads; Representatives Robert Damron, Paul Marcotte, and Jim Wayne.

Guests testifying before the committee: Senator Albert Robinson and Representative Perry Clark, Co-Chairs, Capital Planning Advisory Board; Bill Hintze, Governor's Office for Policy and Management; Jamie Link, Department for Facilities Management; Harold Workman, Kentucky State Fair Board; Gary Cloyd, Kentucky Community and Technical College System; Sandy Williams, Kentucky Infrastructure Authority; George Burgess and Tom Howard, Office of Financial Management; Jim Ackinson, Chief Financial Officer, Kentucky Housing Corporation, Warren Nash, Economic Development Cabinet; and Jennifer Blaser, Peck, Shaffer and Williams, LLP.

LRC Staff: Mary Lynn Collins, Pat Ingram, Nancy Osborne, Kevin Mason, Bart Hardin, and Dawn Groves.

Senator Buford made a motion to approve the minutes of the November 18, 2003, meeting. The motion was seconded by Senator Rhoads and passed by voice vote.

Representative Haydon called on Mary Lynn Collins, Committee Staff Administrator, to review the information items relating to the monthly Lottery report and an update on various capital projects. Included in the update was a note that the Elliott County prison project currently under construction has experienced a rust problem with the stainless steel doors and window frames, and the Finance Cabinet has hired legal counsel regarding that issue.

Representative Haydon then introduced Representative Perry Clark and Senator Albert Robinson, co-chairs of the Capital Planning Advisory Board (Board), to present an overview of the 2004-2010 Statewide Capital Improvements Plan. Joining them was Pat Ingram, staff administrator to the Board. Representative Clark explained the process for development of the biennial report, starting with agency plan submittals in mid-April 2003 and culminating in the November 2003 report. The agency plans report on all projects proposed by any agency for the up-coming six-year cycle including new construction, major renovation or maintenance, equipment, information technology systems, capital grants and loan programs, and court projects. Approximately 1,800 projects were submitted by all three branches for the six-year period and the estimated total of all projects was just over $10 billion with half of that proposed by postsecondary institutions.

The Statewide Capital Improvements Plan has two basic components – policy recommendations and specific project recommendations. Both components focus on maintenance of the state's existing capital assets. Representative Clark stressed that continuing to defer maintenance will cost more in the future.

The 2004-2010 Plan includes nine policy recommendations, some of which have been recommended in prior plans. One recommendation is to establish a statutory mechanism for funding capital renewal and maintenance projects costing over $400,000. Another recommendation addressed adequate and equitable funding for agency maintenance pools for projects costing less than $400,000 each. A third recommendation is to complete implementation of the real properties/facilities management database for the executive branch, as directed by legislation enacted in the 2002 Session. Since the Board is aware that maintenance of state capital assets is also of interest to the Capital Projects and Bond Oversight Committee, the recommendation calls for quarterly progress reports to both the Board and the Committee. The last recommendation to be noted by Representative Clark was for legislation to allow use of the Capital Construction and Equipment Purchase Contingency Fund for moving expenses of state agencies under specific conditions.

Senator Robinson addressed the recommendations for projects for authorization in the 2004-06 budget. The project recommendations fall into three groups: projects to be financed from state funds (General Fund cash or bonds), projects to reduce state leasing of space and facilitate agency consolidations, and projects to be financed from other than state General Fund cash or bonds. During development of the 2004-2010 Plan, the Board has noted a shift in recent budgets away from facilities and infrastructure to deliver state services and programs. Resources have been increasingly focused on projects at the local level. If the shift continues, the Board is concerned that ability to deliver state services will be negatively impacted. The 2004-2010 Plan calls for a balanced approach to the needs and places a high priority on buildings, equipment, and technology to deliver state services and programs. The other focus is on maintenance of existing capital assets, or replacement of such facilities if renovation and repair is not cost efficient or not practicable.

The Plan has seven priority categories, most of which carry a specific dollar value and include specific projects. It is understood that it may not be feasible to fund all projects in each priority category before funding projects in another category. The first priority category is funding of minor projects maintenance pools for agencies and the postsecondary matching pool. The second priority is funding of the statutory pools: the Emergency Repair, Maintenance, and Replacement Fund and the Capital Construction and Equipment Purchase Contingency Fund, and the State-owned Dam Repair Pool. The third priority is to fund capital renewal and major maintenance projects (at least $250 million worth of projects including 24 specific recommendations), and for the projects that further the long-range plan regarding state buildings in Frankfort (renovation of the State Office Building and design of the Capital Plaza Tower renovation). The fourth priority is information technology projects valued at $100 million and including 13 project recommendations. The fifth priority is for approximately $150 million for court projects based on the needs analysis and prioritization of the Administrative Office of the Courts (AOC). The sixth priority is for new construction and grant/loan programs; 16 project recommendations are included in this category. The final priority is completion of the golf courses that were initially authorized in the 1998-2000 budget.

Senator Robinson briefly discussed the other two project types: projects to reduce state leases and facilitate consolidations, and projects to be financed from other than the state General Fund. The Board continues to believe it is important for the state to own more of the facilities it occupies, particularly in Frankfort, to more efficiently and effectively deliver services to the public. Two projects, a federally-funded facility ($11 million) to consolidate offices of the Department for Employment Services and state funds ($61.3 million) for the construction of a state-owned building on state property near the state's central lab, are recommended. The Plan includes selection criteria for projects to be funded by non-General Fund dollars.

Representative Haydon thanked Representative Clark and Senator Robinson for their report and noted the hard work of the Board and its staff. He said he appreciated the concern for funding maintenance needs, and although it is an expensive item, it becomes more expensive when ignored. Representative Wayne also voiced his appreciation for the Board's hard work. He asked if there is an independent body that reviews projects recommended by the AOC. Representative Perry responded that there is an in-house process directed by statute that includes application of detailed standards and criteria. Senator Robinson said it is a very thorough process.

Representative Wayne asked how many of the Department of Military Affairs' projects would be financed by federal funds. Ms. Ingram said that most of the Department's proposed projects involve federal funds and she would get the specific details if desired. Representative Wayne asked if one can tell how much is needed from General Fund cash and from bonds supported by the General Fund. Ms. Ingram responded that the planning process does not distinguish between cash or bonds supported from the General Fund, and that such a financing decision is left to the legislative process. The Plan does include a summary of projects listed by fund source.

Representative Wayne asked about the fund source for the project proposed by the Kentucky State Fair Board. Mr. Harold Workman, President and Chief Executive Officer of the Board, responded that the request to renovate the East Wing/Hall will be for General Fund support. He noted that the currently authorized portion of the renovation is being financed by $51 million in bonds supported by agency receipts, and the Board does not think it has adequate agency receipts to finance another $55 million of bonds needed to finish the renovation.

Representative Haydon introduced and made welcome the new Secretary of the Finance and Administration Cabinet, Mr. Robbie Rudolph, and the Deputy Secretary, Mr. Basil Turbyfill. Next, he asked Mr. Bill Hintze, Governor's Office for Policy and Management, and Mr. Jamie Link, Facilities Management, to make the presentation for the Finance and Administration Cabinet. Mr. Hintze noted that report included seven items submitted by former Cabinet Secretary Gordon Duke.

The first item related to a project authorized by the 1998 General Assembly for the Kentucky State Fair Board to install a floor refrigeration/dehumidification system for a hockey rink in Freedom Hall. Mr. Hintze noted that the project has been completed but does not function adequately, and the state has hired a law firm to seek damages from the vendor. To date, $25,000 has been expended for legal costs from the original project budget, and the request before the Committee is to increase the project's scope by $25,000 (agency receipts) to continue to provide for legal expenses.

Senator Leeper asked if the system is in use at this time. Mr. Workman noted that the system, as currently configured, is cost-prohibitive since it is expensive to freeze the chilled water at an appropriate depth and hot spots are created that can be a safety factor. He added that since there is currently no hockey team, the system is currently not in use.

The second project request reported was from Kentucky State University to use $900,000 in unbudgeted federal funds to purchase a mobile satellite uplink system (truck) for use in the aquaculture program as well as by other cooperative extension programs statewide. The University of Kentucky Cooperative Extension Service sent a letter in support of the project. The project is 100% federally funded.

The third project is a request by the Kentucky Community and Technical College System to use $300,000 in federal funds to equip the Head Start and Daycare Program located in the new facility completed in the Fall of 2003 as the Hindman Branch of the Hazard Community College.

Representative Wayne asked about the history of the project. Mr. Hintze said the facility was initially authorized in the 1998-2000 budget. He said a combination of facility enhancements, not originally planned, developed when federal funds became available. Mr. Gary Cloyd, Kentucky Community and Technical College System, explained that the project was combined with the Knott County Opportunity Center, a federally funded project, in June 2000. In 2001, federal funds became available for a Head Start Program. The revised scope of the project would be $5,056,388.

Representative Damron moved that the three projects reported be approved. The motion was seconded by Senator Rhoads and passed by unanimous roll call vote.

Mr. Hintze said the next three items were informational. The Department of Education reported a change in the roofing projects pool authorized by the General Assembly for the Kentucky School for the Deaf. A new Master Education Facility Plan is currently being developed. Some of the roofs that were scheduled to be repaired are no longer the highest priority. Consequently, the Department has reported that three roof projects have been deleted (Rogers Hall, Old Lee Hall, and Cowan Hall) and two new roof projects added (Grow Hall and Kerr Hall).

Senator Buford said he understood that the Department of Education and the Ephriam McDowell Hospital may be discussing a potential sell of property, and asked if the Finance and Administration Cabinet was aware of those discussions. Mr. Link and Mr. Hintze said they were aware of the discussion, but the buildings just discussed are not related to that discussion.

Mr. Hintze said the second item for the Kentucky School for the Deaf is similar. Moneys initially budgeted for fire safety and dormitory renovation in the Beauchamp, Bruce, Barbee, and Fosdick dormitories will be used on those facilities—even though the operating use of the buildings has changed.

The third information item was a report that two projects at the Southeast Community College, the Belinda Mason Academic/Technical Building project and a pedestrian bridge project across the North Fork of the Kentucky River, have been combined.

The last project presented by Mr. Hintze related to a scope increase of $300,000 in federal funds for the Cabinet for Health Services' Laboratory Information Management System to fully implement the system for a revised scope of $1,075,000. All moneys are from federal Homeland Security grants to states. In response to a question by Representative Wayne, Dr. Rice Leach, Commissioner for Public Health, said that the original $300,000 for the project was allocated in the first year of the grant, and the money for the scope increase now available is from the second year of the grant and was not earmarked for any other use. Representative Marcotte said that he is on a national task force for homeland security and one interest of the group is to use university labs for testing. He asked if university labs will be used in Kentucky for homeland security initiatives. Dr. Leach said that there has been interest in coordinating the state's homeland security efforts with existing university labs such as the Murray State University Breathitt Veterinary Lab in Hopkinsville. Senator Buford moved that the project be approved. The motion was seconded by Senator Rhoads and passed by unanimous roll call vote.

Representative Haydon noted there was a University of Kentucky report in members' folders relating to a recent purchase of an item of scientific equipment for the Ovarian Cancer Screening Program. He noted that no further action was required for the acquisition.

Sandy Williams, Kentucky Infrastructure Authority, next reported six new loans as follows: Paducah/McCracken Joint Sewer Agency, Fund A loan of $1,267,7000 for sewer system upgrades; City of Benton, Fund A loan of $228,886 to construct an interceptor sewer; Cawood Water District, Fund C loan of $500,000 to replace a pump station and storage tank; City of Harlan, Fund F loan of $1,620,000 to expand and upgrade the drinking water treatment plant; City of Eddyville, Fund F loan of $1,718,000 to build a new raw water intake and purchase a water storage tank; and Meade County Water District, Fund F loan of $394,760 to replace water mains and pipes in the Ekron Water Distribution System.

Representative Damron asked about the different rates offered for the loans and how they are set. Ms. Williams explained that for the federally assisted state revolving funds, there is a standard rate of three percent (3%) and a hardship rate of one percent (1%). To qualify for the hardship rate, the median household income must be less than the state's average median household income, and the monthly drinking water rate has to be greater than one and two-tenths percent (1.2%) of the monthly median household income. For the Fund C loans, which do not involve any state funds and are a pooled-loan program, the rate is set by the market at the date of the sale of bonds, but for debt calculation purposes, a conservative approach is used for the financial analysis. For the Cawood Water District loan, the rate is projected at six percent (6%), but will probably be less when the bonds are sold. Representative Damron asked if there is any requirement on an applicant to use KIA funds if the applicant is also receiving state funds. Ms. Williams said there is no requirement to use KIA funds. He asked if an applicant is made aware of other infrastructure loan programs, such as the one offered by the Kentucky Association of Counties (KACO). Ms. Williams said the applicants are made aware of other programs. Senator Moore moved that the projects be approved. The motion was seconded by Representative Marcotte and passed by unanimous roll call vote.

Ms. Williams then reported on several 2020 and Fund B program grants, as well as Coal Development and Tobacco Development grants, that have recently been processed. There were no questions regarding these projects, and no further action was required.

Representative Haydon asked George Burgess, Executive Director of the Office for Financial Management (OFM), and Tom Howard, Deputy Director, OFM, to present new debt issues. Mr. Howard presented the Kentucky Housing Corporation Multifamily Housing Revenue Bonds 2004 Series A to be issued as conduit financing in the amount of $11,800,000 for Falcon Crest Apartments Project, a new 208 unit multifamily complex to be located in Louisville, Kentucky. The expected pricing date is January 7, 2004 with a closing date on or around January 16. The expected ratings are AAA based upon a Fannie May direct-pay letter of credit that will be attached to the transaction. The expected interest rate is 5.15% for up to 33 years. Representative Wayne asked if this was an unusual transaction for the Kentucky Housing Corporation (KHC). Jim Ackinson, Chief Financial Officer, KHC, responded that KHC has not done this type of financing previously. In the past, KHC has done a number of multifamily financings whereby KHC issued the bonds and made the loans on the projects, and held those in a portfolio and made debt service payments on those bonds. KHC has tried to allocate its resources in such a way as to address the needs across the state. He discussed the low income housing tax credit, federal block grants from the Housing and Urban Development agency, the state's Affordable Housing Trust Fund, and tax exempt bonds from the state's private activity bond cap. Over time, most resources are allocated to the single family homeownership program, KHC's benchmark program. For the past several years, KHC has offered the product of financing multifamily projects targeted to the urban parts of the state. A unique aspect of the multifamily bond program is that the state automatically gets additional tax credits above the state's annual allocation although at a lower rate. KHC thinks it is more efficient to offer this new program on a conduit basis, and this project is KHC's first attempt to do that. KHC will not be taking a risk as part of the underwriting on the loan – it will allow the private sector to do that. KHC will do some "due diligence" and expect the development meets other KHC criteria, but will otherwise be an issuer in name only.

Representative Wayne noted that the development is in his district and asked whether it is good state policy to put 208 units of low-income households in one spot. Mr. Ackinson said the state would want the local community to make that decision. Representative Wayne asked who made that local decision here. Mr. Ackinson replied that they are seeking a letter of support from the Mayor of Louisville on behalf of the Jefferson-Louisville Metropolitan Government. Representative Wayne asked that the Committee get a local letter of support prior to further Committee action and moved to defer action until the next meeting. Representative Marcotte seconded the motion.

Representative Damron asked for further discussion and said he was not against the motion. He asked why is KHC serving as a conduit rather than the City of Louisville. Mr. Ackinson said that the City of Louisville could go through the 2004 private activity bond cap process to get a local issuer cap and go through the inducement resolution process at the local level and issue the bonds in that manner.

Representative Damron asked when a private developer issues bonds through KHC, does it fall under all procurement laws and prevailing wages. Mr. Ackinson said he could not address that. Representative Damron said he would like to get these questions, and the ones raised by Representative Wayne, answered before he voting on the project.

Representative Haydon directed staff to develop a list of questions on behalf of the Committee to KHC. The motion to defer was adopted by unanimous voice vote.

Mr. Howard next presented a new bond issue: Kentucky Economic Development Finance Authority (KEDFA) Hospital Facilities Revenue Refunding Bonds, Series 2003 for AHF/Kentucky-Iowa, Inc. ($4,391,000). Mr. Howard explained that KEDFA is serving as a "conduit" for the bonds so they can be issued at a tax-exempt rate. The new issue will refund and retire outstanding bonds from which the proceeds were originally used to finance the acquisition of two health care facilities in Lexington and Louisville. He noted that the issue's bond counsel, Jennifer Blaser with Peck, Shaffer and Williams, LLP, was present to respond to questions. In response to questions from Representative Damron, Mr. Howard explained that AHF/Kentucky-Iowa Inc. has filed for bankruptcy, and the holders of the prior bonds have agreed to exchange the prior bonds for the new ones and to a reduction of $5.2 million in asset value as part of the reorganization.

Representative Damron asked about the estimated savings from the bond issue. Ms. Blaser responded that there are no savings, that the issue is a restructuring of the debt to lower the payments for the next five years.

In response to a question from Representative Wayne, Ms. Blaser indicated that the issue is a conduit and the Commonwealth is not at risk. The sole responsibility for repayment of the bonds rests with AHF/Kentucky-Iowa, Inc.

Representative Damron asked if KEDFA was the original issuer. Ms, Blaser said there were two original issuers: Lexington-Fayette Urban County Government and Jefferson County. She noted that because there are multiple sites, the company had requested KEDFA to issue the conduit. She noted that there are cost savings by putting the two issues together.

In response to another question by Representative Damron, Ms. Blaser said the issue does not affect KEDFA's debt capacity.

Warren Nash, Deputy Commissioner for the Department for Financial Incentives, Economic Development Cabinet, told the committee that both the Jefferson-Louisville Metropolitan Government and the Lexington-Fayette Urban County Government asked KEDFA to participate in the issue.

Senator Leeper indicated that he was going to make a motion to approve the project, but that the Committee had some concern that KEDFA has not been submitting follow up reports on bond sales in a timely fashion. He said he wanted to start a new process today in regard to approvals of KEDFA issues and then made a motion to approve the KEDFA Health Care Facilities Revenue Refunding Bonds, Series 2003 contingent up the Committee receiving a follow-up report as soon as the issue is sold. The motion was seconded by Representative Wayne and passed unanimously by a roll call vote.

Mr. Burgess then reported on six follow-up reports (approval letters) for previously approved bond issues: Kentucky Housing Corporation Housing Revenue Bonds, 2003 Series D (AMT) and Series E (AMT) Variable Rate; Kentucky State Property and Buildings Commission Agency Fund Revenue Bonds, Project No. 81, University of Kentucky Consolidated Educational Buildings Refunding Revenue Bonds, Series O (Second Series); University of Kentucky Consolidated Educational Buildings Refunding Revenue Bonds, Series T; University of Kentucky Housing and Dining System Refunding Revenue Bonds, Series M and O (Second Series); and University of Louisville Consolidated Educational Buildings Revenue Bonds, Series O. Representative Haydon said that these issues were approved at an earlier committee meeting and did not require further action.

Representative Haydon said the next items on the agenda are follow up reports of KEDFA issues. He said that the reports are dated, one of the issues is over a year old, the rest are four to six months old. While no further action was required, he asked that in the future the follow up reports on KEDFA issues be filed in the same manner as other bond issues.

Mr. Nash said that both his office and OFM had been frustrated by the delays in obtaining these reports and that the committee's action on the AFH/Kentucky-Iowa Inc. project—giving approval contingent upon a follow-up report being sent as soon as the bonds are sold—will give his office a "stick" to use to get that report to the Committee in a timely manner. He noted for the Committee that the KEDFA issues are different from other state bond issues in that no state funds are associated with the issues. However, he said that the statute requires timely follow-up reports, and it would be helpful to his office if the Committee tied all future KEDFA bond approvals contingent upon receipt of timely follow up reports.

Mr. Burgess then reviewed certification sent to the Committee that neither he or former Finance Secretary Gordon Duke were involved in any way with the selection of underwriters' counsel for State Property and Buildings Commission Bonds Projects No. 77, 78, 79, 80 Series A, and 81. He then presented five new school bond issues with School Facilities Construction Commission participation: Bardstown Independent, Breckinridge County, Letcher County, Mason County, and Wolfe County. He said there are no tax increases associated with any of these issues.

Senator Moore made a motion to approve the six school bond issues. The motion was seconded by Representative Marcotte and passed by a roll call vote. Six members voted affirmatively and Representative Damron abstained from the vote, citing a potential conflict of interest.

Representative Haydon said there were two locally funded school bond issues submitted to the committee for review this month: Madison County and the Kentucky Interlocal School Transportation Association. He said all disclosure information has been filed, and no further action on the bond issues is required.

Representative Haydon said the committee will hold its next meeting on January 20.
With there being no further business, Representative Damron made a motion to adjourn the meeting. The motion was seconded by Senator Moore. The meeting adjourned at 2:27 p.m.